



Statement of the U.S. Chamber of Commerce

ON: CHALLENGES TO EMPLOYER EFFORTS TO PRESERVE
RETIREE HEALTH CARE BENEFITS

TO: HOUSE SUBCOMMITTEE ON EMPLOYER-EMPLOYEE
RELATIONS

BY: STEVEN D. SPENCER

DATE: APRIL 28, 2005

The Chamber's mission is to advance human progress through an economic,
political and social system based on individual freedom,
incentive, initiative, opportunity and responsibility.

Statement of Steven D. Spencer
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on behalf of the
United States Chamber of Commerce
before the
Subcommittee on Employer-Employee Relations
of the
Committee on Education and the Workforce
United States House of Representatives

“Challenges to Employer Efforts to Preserve Retiree Health Care Benefits”

April 28, 2005

10:30 AM

Chairman Johnson and members of the subcommittee, I am pleased and honored to be here today. Thank you for your kind invitation.

By way of introduction, I am a partner at the law firm of Morgan, Lewis & Bockius LLP. I work in Philadelphia, Pennsylvania, where the United States Court of Appeals for the Third Circuit—the court that issued the *Erie County* decision in 2000—resides. My practice focuses on advising single-employer and multi-employer benefit plans, i.e., those managed jointly by employers and unions, regarding employee benefit matters. I have been practicing in this area of law since 1978. In my spare time, I am a lecturer at the University of Pennsylvania Law School and an adjunct professor of law at the Villanova University Law School where I teach courses on employee benefit law. I am testifying today on behalf of the U.S. Chamber of Commerce.

I am sure that you are aware of the spiraling cost of health care coverage in this country. A nationwide survey of large employers found that the cost of providing retiree health benefits increased by an estimated 12.7 percent on average between 2003 and 2004 alone. The Henry J. Kaiser Family Found. & Hewitt Assocs. LLC, *Current Trends and Future Outlook for Retiree Health Benefits* (Dec. 2004), at 9. The experiences of our clients bear out the conclusions of the many studies that have found that the steadily rising costs of health care, changes in the accounting rules and rising pension costs have placed employers and organized labor under ever-increasing pressure to reduce expenditures on all benefit programs—including retiree health benefits. For example, a recent study suggests that if current trends continue, the employer-share of health benefit costs could increase by more than 236 percent between 2002 to 2010. Employment Policy Foundation, *Employer's Share of Health Benefit Costs Could Top \$10,000 per Employee by Decade's End* (May 1, 2003). This pressure has forced plan sponsors to constantly reexamine the coverage provided to employees and retirees in order to remain competitive in local and global markets. Today, plan sponsors face the same pressures that led Erie County to restructure its plans and to the Third Circuit decision that has resulted in today's important hearing. To fully understand the impact of the *Erie County* decision on future retiree health benefits, it is important to understand the history of retiree health coverage in this country.

Background on Retiree Health Care

For decades, employers and unions have taken Medicare eligibility into account when designing and implementing retiree health benefit plans. These plans have

generally provided one of two forms of benefits, or both: (1) “Medicare Bridge” benefits for early retirees, which typically continue the same health benefits as are provided for active employees until the retiree becomes eligible for Medicare; and (2) Medicare supplement or carve out plans for retirees who are eligible for Medicare. Like many plan sponsors, Erie County provided its retirees who were not Medicare-eligible with “Medicare Bridge” benefits and its Medicare-eligible retirees with a Medicare supplemental plan. This plan design was widely regarded as legal under the Age Discrimination in Employment Act (ADEA)—the federal statute that bars employment discrimination based on age—until 2000 when the Third Circuit Court of Appeals changed the status quo with its decision in *Erie County*.

Background of *Erie County* Case

Faced with increasing health insurance costs, the Erie County Employees’ Retirement Board (the Board), which administered the medical coverage, decided that employees hired after January 23, 1992, would not be eligible for continued health insurance benefits upon retirement. On December 12, 1995, the Board further restricted eligibility by declaring that persons the county hired prior to January 23, 1992, would remain eligible only if they fell into one of four groups: (1) employees unable to continue their employment due to a disability, who otherwise were eligible for a disability retirement pension; (2) employees who retired from the county government with at least 20 years of service and 55 years of age; (3) employees involuntarily terminated from county government employment with at least eight years of service; and (4) employees who retired from the county with at least eight years of service and 60 years of age. Prior

to 1998, all county employees and retirees were covered by traditional indemnity plans. With health care costs still increasing and a change in financial accounting standards, the county announced late in 1997 that going forward Medicare-eligible retirees would be covered by an HMO Medicare supplement that required coordination of all health care by a primary care physician, while early retirees would be covered by a point-of-service plan. A group of Medicare-eligible retirees sued their former employer, alleging that Erie County discriminated against its older retirees in violation of the ADEA because the HMO Medicare Supplement required retirees to coordinate their medical care through a primary care physician, while younger retirees under the point-of-service plan were not required to coordinate their benefits through a primary care physician. The Third Circuit Court of Appeals found that this plan design violated the ADEA unless Erie County could show that it could satisfy the ADEA's "equal cost/equal benefit" defense. Directed to come into compliance, Erie County ultimately equalized the retiree health benefits it offered the only way that it could afford to—not by improving the benefits for its Medicare-eligible retirees—but by reducing the level of health care benefits offered to early retirees.

Impact of *Erie County* Decision

Following the *Erie County* decision, many clients asked whether they should terminate their retiree health plans that were at risk. Until recently, we have advised that while they are at risk, rather than terminate their plans, they should consider a "wait and see" approach to see how the other Circuits and the EEOC would react, particularly because the EEOC had announced that it would promulgate a narrow exemption to the

ADEA, which would recognize that plans could continue offering Medicare-coordinated retiree health benefits. However the legal landscape changed on March 30, 2005, when Judge Brody of the Eastern District of Pennsylvania permanently enjoined the EEOC from issuing the exemption. Once again plan sponsors have asked whether they should terminate their plans.

According to the Third Circuit, the only way that a plan sponsor can justify providing different benefits to Medicare-eligible retirees as compared to younger retirees would be to meet the “equal benefit or equal cost” test established in Section 4(f)(2) of the ADEA and EEOC regulations. To do so, the plan sponsor would have to show either (1) that the benefits provided to Medicare-eligible retirees (factoring in Medicare) were equal or better than those offered to early retirees or (2) that it spent the same amount buying health insurance for each retiree, without considering the value of the Medicare benefit. As illustrated by the *Erie County* case, subtle differences in the benefits provided to pre- and post-Medicare-eligible retirees may be found by a court to violate the equal benefit test. Moreover, plan sponsors may be unable to demonstrate that they satisfy the equal cost test where they provide a Medicare carve-out or Medicare supplement plan, because Medicare will bear a substantial portion of the cost.

The problem with the *Erie County* decision is that, given the rapidly escalating costs of health care, it leaves plan sponsors with few options other than to restructure and reduce the health benefits provided to retirees. Plan sponsors can comply with the *Erie County* decision only by: (1) increasing health benefits for retirees over the age of 65; (2) reducing health benefits for retirees under the age of 65 to match those provided by Medicare; (3) limiting the duration of health benefits to a specified number of years

regardless of age; or (4) terminating health benefits for all retirees. In light of the ever-increasing cost pressures on plan sponsors, few would choose to raise the benefit levels for post-65 retirees, opting instead to reduce or eliminate retiree health benefits.

It is estimated that more than 3 million retirees between the ages of 55 and 64 rely on employer-sponsored plans for their health insurance coverage, while about 11 million people over the age of 65 have supplemental coverage from an employer-sponsored plan. *See* Statement of Patricia Neuman to the U.S. Senate Special Committee on Aging, May 17, 2004 (Exhibits 1 and 2). For early retirees, employer-sponsored plans generally provide access to relatively affordable and comprehensive coverage. Without this coverage, many retirees who are pre-65 and too young for Medicare would be hard-pressed to find comparable, affordable coverage on their own. While Medicare-eligible retirees, unlike early retirees, have Medicare as their primary source of health insurance, many rely on employer-sponsored retiree plans to provide needed assistance in supplementing Medicare's benefits.

Why the EEOC Exemption Is Appropriate

Retiree benefits are not like other forms of compensation for employees, and therefore should be approached differently when evaluating age discrimination concerns. First, our society has in place certain protections for retirees age 65 or older that are not available to younger retirees, e.g., Social Security and Medicare. Second, we are talking only about retirees, not employees. No one is suggesting that employees should be treated differently based on their age. With regard to retirees, however, the law, recognizing the existence of protections such as Social Security and Medicare, already

permits distinctions that favor younger retirees. For example, Section 4(l) of the ADEA and Section 204(b)(1)(G) of the Employee Retiree Income Security Act (ERISA) both explicitly permit employers to pay subsidized early retirement benefits to retirees until they are eligible to receive Social Security. *See* 29 U.S.C. § 1054. These bridge benefits permit employees to retire early and receive a subsidized benefit that disappears when the employee becomes eligible for Social Security. These “Social Security Bridge” benefits are particularly important when employees are terminated, as businesses downsize and restructure. But early retirees will face severe hardships if the law prohibits “Medicare Bridge” benefits. The fact is that most employees cannot retire before age 65 unless they have medical insurance to cover them until Medicare is available. For most retirees, buying individual coverage is cost prohibitive. For a couple age 55, one year’s health care insurance this year could easily reach or exceed \$8,400,¹ rising at 13 percent per year. The cost for that couple to purchase coverage until they qualify for Medicare at age 65 would total more than \$175,000 if medical costs continue to increase at only 13 percent per year.

Plan sponsors want to ensure that adequate health benefits are available to their employees upon retirement. That’s why labor and management support the EEOC exemption, which would remove a significant obstacle to achieving that goal. The EEOC exemption, if implemented, would preserve Medicare Bridge benefits. In the absence of the proposed exemption, plan sponsors will either terminate their retiree health plans or structure them in a way that reduces the level of benefits to early retirees while producing no additional benefits to Medicare-eligible retirees. The EEOC exemption merely recognizes the reality that an interpretation of the ADEA that would result in a net loss of

¹ Quote obtained from www.ehealthinsurance.com.

employer-sponsored retiree health benefits does not promote the purposes of the ADEA and is not in the public interest.

Mr. Chairman and members of the subcommittee, thank you for the opportunity to testify today and for your attention to this very important issue. I would be happy to answer any questions that you might have.

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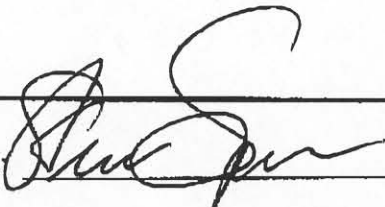
Committee on Education and the Workforce

Witness Disclosure Requirement – “Truth in Testimony”

Required by House Rule XI, Clause 2(g)

Your Name: Steven D.Spencer		
1. Will you be representing a federal, State, or local government entity? (If the answer is yes please contact the Committee).	Yes	No X
2. Please list any federal grants or contracts (including subgrants or subcontracts) which <u>you</u> have received since October 1, 1998: None		
3. Will you be representing an entity other than a government entity?	Yes x	No
4. Other than yourself, please list what entity or entities you will be representing: U.S. Chamber of Commerce		
5. Please list any offices or elected positions held and/or briefly describe your representational capacity with each of the entities you listed in response to question 4: Client		
6. Please list any federal grants or contracts (including subgrants or subcontracts) received by the entities you listed in response to question 4 since October 1, 1998, including the source and amount of each grant or contract: None		
7. Are there parent organizations, subsidiaries, or partnerships to the entities you disclosed in response to question number 4 that you will not be representing? If so, please list:	Yes	No x

Signature



Date:

4/27/05